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CABINET AFFAIRS STAFFING MEMORANDUM

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Date: 1/18/84 **Number:** ---------- **Due By:**

Subject: Cabinet Council on Economic Affairs Minutes - January 5, 1984

	Action	FYI
ALL CABINET MEMBERS	☐	☑
Vice President	☐	☐
State	☐	☐
Treasury	☐	☐
Defense	☐	☐
Attorney General	☐	☐
Interior	☐	☐
Agriculture	☐	☐
Commerce	☐	☐
Labor	☐	☐
HHS	☐	☐
HUD	☐	☐
Transportation	☐	☐
Energy	☐	☐
Education	☐	☐
Counsellor	☐	☐
OMB	☐	☐
CIA	☐	☑
UN	☐	☐
USTR	☐	☐
GSA	☐	☐
EPA	☐	☐
OPM	☐	☐
VA	☐	☐
SBA	☐	☐

	Action	FYI
CEA	☐	☑
CEQ	☐	☐
OSTP	☐	☐
Baker	☐	☑
Deaver	☐	☑
Darman *(For WH Staffing)*	☑	☐
Jenkins	☐	☑
Mc Farlane	☐	☑
Svahn	☐	☑
CCCT/Gunn	☐	☑
CCEA/Porter	☐	☑
CCFA/	☐	☑
CCHR/Simmons	☐	☑
CCLP/Uhlmann	☐	☑
CCMA/Bledsoe	☐	☑
CCNRE/	☐	☑

REMARKS:

Attached for your information are the minutes of the January 5, 1984 CCEA meeting.

DCI EXEC REG

RETURN TO:

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MINUTES
CABINET COUNCIL ON ECONOMIC AFFAIRS

January 5, 1984
8:45 a.m.
Roosevelt Room

Attendees: Messrs: Regan, Block, Baldrige, Donovan, Feldstein, Porter, Abrams, Ballentine, Poole, Sprinkel, Wallis, Cicconi, Gibson, Hamburger, Verstandig, Courtemanche, and McAllister.

1. Financial Market Developments and Monetary Policy

The Council reviewed papers prepared by Under Secretary of the Treasury Beryl Sprinkel, Council of Economic Advisers Member William Poole, and Office of Management and Budget Associate Director Gregory Ballentine. Mr. Poole stated that the increases in interest rates in recent weeks are normal when measured against previous recoveries and do not represent a reversal of the gains achieved in bringing rates down over the past three years. He noted that the markets had previously speculated that the Federal Reserve would act to lower interest rates. However, in recent weeks, analysts have been persuaded that the Federal Reserve is not attempting to lower interest rates, but may instead actually be pushing rates higher.

Mr. Poole stated that in his view the velocity of money will increase sharply over the first half of 1984. Based on a five percent annual growth in the money supply, he estimates a velocity of 4 to 5 percent in 1984, resulting in nominal GNP growth of 9 percent to 10 percent, which is consistent with the Administration's forecast of 9.7 percent growth. He noted however that, in his opinion, future money growth is uncertain because the Federal Reserve is targeting interest rates. By attempting to stabilize interest rates, the Federal Reserve surrenders control of the money supply. He stated that in his view the Administration should emphasize to the Federal Reserve the importance of controlling the money supply, while accepting the greater interest rate variability that will result from this policy. He suggested that if the 2 to 3 percent growth in the money stock of the last few months continues, a recession in 1984 would be likely.

Mr. Ballentine stated that the question of whether the Federal Reserve should change or maintain its current policy depends in part on the interpretation of the money supply data of the past few months. He explained that the Federal Reserve's seasonal

adjustment factors change from year to year. Comparing the money supply numbers for 1983 adjusted by the 1983 adjustment factors with the same numbers adjusted by the 1982 adjustment factors reveals significant differences. He stated that the variability of the seasonal adjustment factors suggests caution should be used in interpreting money growth over short periods of time.

Mr. Ballentine stated that alternative measures of money growth, such as the monetary base, which has growth at a consistent 8 percent rate, suggest that the decline in the M1 estimates may be exaggerated. He suggested that the Administration express its support for the Federal Reserve's current policy.

Mr. Sprinkel stated that, in his opinion, if the low rate of money growth continues, a recession is possible in the second or third quarter of 1984. He pointed out that changes in the growth rate of M1 are closely correlated with changes in industrial production in the short term. He observed that sharp contractions in the money supply have typically preceded recessions. He noted that in recent weeks M1 has shown significant positive growth, but weekly money supply data are notoriously erratic.

The Cabinet Council's discussion focused on a number of topics, including the effect of financial deregulation on the velocity of money. Mr. Poole stated that the change in the velocity of money due to financial deregulation is much less significant that the rate of growth of M1. The primary issue is the Federal Reserve's policy of stabilizing interest rates. The Council also noted that M2 is not a good alternative indicator of the money supply. There was no importation deceleration of M2 preceding the 1981-82 recession, nor did it predict the acceleration of inflation in 1978-81 or the deceleration in 1982-83. The Council agreed that the most desireable rate of growth of M1 should be 5 to 6 percent, the lower range of the Federal Reserve's 5 to 9 percent target range.

The Council requested the Working Group on Financial Market Developments and Monetary Policy to investigate the worldwide increase in the demand for currency.